IN THE HIGH COURT OF GUJARAT AT AHMEDABAD

INCOME TAX REFERENCE No 119 of 1987

For Approval and Signature:

Hon'ble MR.JUSTICE A.R.DAVE
and
Hon'ble MR.JUSTICE D.A.MEHTA

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1. Whether Reporters of Local Papers may be allowed to see the judgements? : YES

2. To be referred to the Reporter or not? : YES

3. Whether Their Lordships wish to see the fair copy of the judgement? : NO

4. Whether this case involves a substantial question of law as to the interpretation of the Constitution of India, 1950 of any Order made thereunder? : NO

5. Whether it is to be circulated to the Civil Judge? : NO

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COMMISSIONER OF INCOME TAX

Versus

RAMLUBHAIYA R MALHOTRA

Appearance:

1. INCOME TAX REFERENCE No. 119 of 1987

MR AKIL QURESHI for MR MANISH R BHATT for Petitioner No. 1

MR RK PATEL for the Respondent

CORAM : MR.JUSTICE A.R.DAVE
and
MR.JUSTICE D.A.MEHTA

Date of decision: 13/08/2001

ORAL JUDGEMENT

(Per : MR.JUSTICE D.A.MEHTA)

The Income Tax Appellate Tribunal, Ahmedabad Bench 'C', has referred the following question for the opinion of this Court :

"Whether the Tribunal was right in law and on facts in upholding the claim of the assessee for depreciation u/s 34(2)(ii) specially when the proprietary business was converted into a partnership firm during the relevant accounting period?"

2. The Assessment Year is 1977-78 and the accounting period is Financial Year 1976-77. The assessee was running a proprietary business in the name of Standard Rolling Mills and the said business was conducted for the period 1.4.1976 to 30.6.1976 during the financial year. With effect from 1.7.1976 the business, with all its assets and liabilities, was taken over by a new firm having the same business name. The assessee's share in this partnership firm was 40 per cent. The assessee claimed depreciation and investment allowance as deduction against the profits from the proprietary business, which was carried on during the part of the year. The assessee's claim was rejected by the Assessing Officer. The CIT (Appeals) allowed the assessee's appeal holding that the assessee was entitled to both investment allowance and depreciation as claimed.

3. The revenue went in appeal before the Tribunal and the Tribunal, for the reasons stated in its order dated 29.11.1985, allowed the appeal of the revenue in part by holding that the assessee's claim for investment allowance was not justified. Insofar as the claim for depreciation was concerned, the order of CIT (Appeals) was affirmed by the Tribunal. It appears from the facts on record that the assessee has accepted the finding of the Tribunal as regards the disallowance of its claim for investment allowance, while the revenue has preferred the present reference in relation to the claim for depreciation, which has been allowed by the Tribunal.

4. We have heard both Shri Akil Qureshi appearing for the revenue and Shri R.K. Patel appearing on behalf of the assessee. We do not find any justifiable reason to interfere with the findings recorded by the Tribunal.

5. Depreciation is nothing else but a legislative provision made for normal wear and tear of the assets used in the course of business from which profits liable

to tax are earned. It is an undisputed fact that profits of the proprietary concern for the period during which it functioned have been brought to tax. Section 34(2)(ii) of the Income-tax Act, 1961 (hereinafter referred to as 'the Act'), on which reliance was placed on behalf of the revenue, cannot be invoked for the simple reason that it envisages a denial of claim for depreciation only in those cases where the assets are "sold, discarded, demolished, destroyed". Admittedly, in the present case it cannot be contended that the assets in question were either discarded or demolished or destroyed. The revenue's case rests only on the aspect of "sale" of proprietary business to partnership firm. The settled legal position is that, under the partnership law, when the assets of a proprietary business are brought as capital contribution in the partnership firm, there is no sale inasmuch as the proprietor-assessee, who becomes a partner of the firm, retains his interests in the assets. Thus, the situation envisaged by the use of the term 'sold' cannot be applied to the case of the assessee. The Tribunal has also taken into consideration the definition of 'sold' under Explanation (2) to sec. 32(1)(iii) of the Act and come to the conclusion that, though the expression 'sold' is an inclusive definition, it includes transfer only by way of exchange or compulsory acquisition under any law and on facts there is neither exchange nor any compulsory acquisition. It has, therefore, been held that even the inclusive definition of the expression 'sold' cannot be applied to the facts of the case.

6. Insofar as the definition of 'transfer' given within the meaning of sec. 2(47) of the Act is concerned, it is apparent that the said definition is applicable only in case of transfer of a capital asset for the purposes of computation of capital gains, and thus the extended definition of transfer cannot be made applicable in the present case.

7. The Madras High Court in the case of A.M. Ponnurangam Mudaliar v. CIT & Anr., 228 ITR 454, has adopted the same view and we are in respectful agreement with the same.

8. We, therefore, hold that the Tribunal was justified in law in upholding the claim of the assessee for depreciation under sec. 34(2)(ii) of the Act in a case where the proprietary business was converted into a partnership firm during the relevant accounting period. The question referred to us is, therefore, answered in the affirmative, that is, in favour of the assessee and

against the revenue.

The referene stands disposed of accordingly with no order as to costs.

(A.R. Dave, J.)

(D.A. Mehta, J.)

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